State of California

660.0060

Memorandum

To : Mr. Verne Walton

Date : December 18, 1985

From : Eric F. Eisenlauer

Subject : Existence of Taxable Possessory Interest at United States Marine Corps Base at Camp Pendleton

This memo is in reply to your memo to Mr. Richard Ochsner of November 13, 1985 in which you, in effect, ask whether a taxable possessory interest was created by the contract between the United States Marine Corps Exchange ("the Exchange") and G. T. Tucker Inc., a licensed franchisee of McDonald's Corporation, ("the Contractor") to operate a McDonald's restaurant in Building #1101 at Camp Pendleton.

In determining the existence of a taxable possessory interest, the situation must be measured by an objective standard rather than by accepting the literal language of the written instrument as controlling the nature of the relationship established. Because of the variety of interests that may be created by agreements, the question of whether a taxable possessory interest has been created must be decided on a case-by-case basis by weighing the factors of durability, exclusiveness, private benefit and independence. In each case, judgment is to be made by an examination of the agreement in its entirety. (Stadium Concessions, Inc. v. City of Los Angeles (1976) 60 Cal.App.3d 215; Wells National Services Corp. v. County of Santa Clara (1976) 54 Cal.App.3d 579; Mattson v. County of Contra Costa (1968) 258 Cal.App.2d 205; see also Property Tax Rule 21(a)(1).) In order to determine whether a taxable possessory interest has been created in this case, it is necessary to analyze the Contract in light of the standard set forth above.

Durability

To satisfy the requirement of durability, the agreement must confer use for a determinable period and the use has to be reasonably certain to last for that period. (Kaiser v. Reid (1947) 30 Cal.2d 160.) If the agreement provides for cancellation on short notice as the Contract in this case does (¶¶ 14 & A-25), the past history of dealings between the parties may supply sufficient durability. (Freeman v. County of Fresno (1981) 126 Cal.App.3d 459 at p. 463.)

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Here the Contract became effective October 4, 1982 (¶ 12). The term of the Contract is for one year commencing the date an addendum to the Contract is signed indicating the acceptance of the remodeled facilities by the Base Public Works Officer and the Exchange (¶ 12). The Contract provides for extension for four additional one year periods upon mutual consent of the parties (¶ 13). In view of the provisions for remodeling to prepare the premises for the operation of fast food service (¶ 6); the acquisition of equipment, decor and furnishings (¶¶ 7, 8, attachment C), the cost of which was all borne by Exchange; and considering the fact that the Contract has already been in effect more than three years, it seems reasonable to assume that the Contract will remain in effect at least five years. Such a term is of sufficient duration to satisfy the factor of durability (Mattson v. County of Contra Costa, supra, at p. 211).

Exclusiveness

The test for exclusiveness is not exclusive possession against all the world including the owner. (Wells, supra, at p. 584.) The right of use, however, must carry with it the degree of exclusiveness necessary to give the user something more than a right in common with others. (United States of America v. County of Fresno (1975) 50 Cal.App.3d 633, 638.) To be exclusive, such use "must not be one shared by the general public and, at least until cancelled, must be enforceable against the public entity which permits the use." (Freeman v. County of Fresno, supra, at pp. 463, 465; see also Property Tax Rule 21(e).)

The Contract in this case provides that the "Contractor shall have exclusive control over food preparation and all other facility operations subject to Base Sanitation regulations, and Exchange inspection for compliance with the terms of the Contract" (¶ 3). There is nothing in the Contract to suggest that Contractor's right of use of the premises is anything less than the degree of exclusiveness required by the cases cited above.

Although it might be argued based on Pacific Grove-Asilomar Operating Corp. v. County of Monterey (1974) 43 Cal.App.3d 675 that Contractor does not have exclusive use of the premises because it is open to the general public (to the extent the general public has access to Camp Pendleton), that case is factually distinguishable from this one. In that case, Asilomar was a nonprofit corporation organized and established solely to manage the state-owned conference grounds in question and derived no private benefit from the management of the property. In holding that no taxable possessory interest existed, the court noted (at p. 695) that "the fact that the relationship between Asilomar and the state has no profit motive is an element material in determining the nature of Asilomar's interest."

In this case, there clearly is a profit motive as Contractor is entitled to 47.5 percent of the gross sales receipts under the terms of the Contract (¶ B-8). In the similar commercial setting involved in Mattson, supra, access of the general public (to the dining area of a public golf course operation) was held not to detract from the element of exclusiveness of possession or use (Mattson, supra, at p. 210).

Based on the foregoing, we believe the requirement of exclusiveness is satisfied.

Private Benefit

The requirement of private benefit is met if there is an opportunity for the holder of the interest to make a profit. (Wells Nat. Services Corp. v. County of Santa Clara, supra, at p. 585.) Contractor clearly has an opportunity to make a profit through its use of Exchange property under the Contract in this case in that it is entitled to receive 47.5 percent of the gross sales receipts from the operation of the fast food facility (¶ B-8). The private benefit requirement is therefore clearly satisfied.

Independence

To qualify as a possessory interest, the right to use property must be sufficiently exclusive, durable and independent of the public owner to constitute more than an agency. (Pacific Grove-Asilomar Operating Corp. v. County of Monterey, supra, at p. 684.) "If, in practical effect, one of the parties has the right to exercise complete control over the operation, an agency relationship exists;..." (Nichols v. Arthur Murray, Inc. (1967) 248 Cal.App.2d 610, 613.) As a general proposition, if exclusiveness and private benefit are present, the other requirements (durability and independence) are usually found to exist as well. (See Freeman v. County of Fresno, supra, at p. 463.)

With respect to the question of whether an agency relationship exists in this case, the Contract is explicit. It provides at Paragraph 13 of Attachment "A" that "[t]he operation hereunder, performed on the military installation by the Contractor,...shall be under the supervision and control of the Exchange, and shall be subject to the provisions of all applicable regulations or directives now in effect or thereafter promulgated,...provided, however, <u>that under no circumstance shall the Contractor and any of his employees or agents be deemed to be the employees or agents of the Exchange or the United States</u>...." (Emphasis added.)

Although the foregoing language is not necessarily controlling as pointed out above, it does indicate that no agency relationship exists between the Exchange and the Contractor.

Other provisions of the Contract support that conclusion. For example, the methods of operation, logo, uniform dress, distinctive color schemes, etc. are to be substantially identical to those standards established by Contractor's operation in the civilian community. Further, Contractor is to have exclusive control over food preparation and all other facility operations subject to Base sanitation regulations and Exchange inspection for compliance with the Contract terms (¶¶ 3, B-1).

With respect to remodeling of the facilities (which presumably has long since been completed), Contractor had the responsibility for the interior design and color scheme of the building; was required to provide the plans and specifications for all physical remodeling; and was obligated to act as Architectural Engineer and General Contractor. All remodeling work was to be supervised and inspected by a qualified inspector employed by Contractor. Exchange was to bear the cost for remodeling (¶ 6).

With respect to equipment and furnishings, Contractor was and is responsible for procuring and installing all equipment, decor and furnishings on behalf of and subject to the approval of Exchange. All costs are to be borne by Exchange (¶¶ 7, 8). With respect to the employees which operate the fast food operation, it is the Contractor's obligation to pay all salaries, benefits, costs and expenses associated with its employees in the fast food facility including training (¶ 11).

Paragraph 10 of Attachment A requires the Contractor to indemnify and hold harmless the Exchange and the United States from damages. Such a provision is indicative of independent operation (<u>Mattson</u> v. <u>County of Contra Costa</u>, <u>supra</u>, at p. 211).

Further, the Contract contains a covenant against assignment without written consent (¶ 16) which, although not conclusive, "is frequently characteristic of leases and is inconsistent with mere license" (Mattson, supra, at p. 211). On the whole, the arrangement between Contractor and Exchange is similar in many respects to the one between the City of Concord and the restaurant concessionaire in Mattson, supra, wherein the court found that the operation was "much too autonomous to be regarded as a mere agency."

We recognize there are differences here which make this a closer case than Mattson. For example, Exchange retains the sole right to establish retail prices (¶ 5). Also, it bears the cost of food products and related items (¶ B-1). On balance, however, we are of the opinion that based on the Contract in its entirety, no agency relationship exists between Contractor and Exchange and the requirement of independence is therefore satisfied. Moreover, even if Contractor's independence here were in doubt, there is recent authority to the effect that independence from public control is not necessary for taxability (Freeman v. County of Fresno, supra, at p. 465).

In summary, it appears that Contractor's right to use Exchange property under the Contract meets the requirements of durability, exclusiveness, private benefit and independence. Accordingly, it can reasonably be concluded that Contractor's right is a taxable possessory interest.

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cc: Mr. Gordon P. Adelman
Mr. Robert H. Gustafson